FLH ICT SERVICES SDN BHD & ANOR v. MALAYSIAN DEBT VENTURES BHD

COURT OF APPEAL, PUTRAJAYA
VARGHESE GEORGE JCA
AHMADI ASNAWI JCA
PRASAD SANDOSHAM ABRAHAM JCA
[CIVIL APPEAL NO: W-02 (MUA)(W)-704-04-2014]
13 NOVEMBER 2015

BANKING: *Banking facility – Islamic financing – Bai' al-inah – Asset sale agreement and asset purchase agreement – Recovery of money due and payable – Failure to state asset used in transaction – Whether bai' al-inah contract in compliance with Syariah principle of financing*

CIVIL PROCEDURE: *Appeal – Appeal against judgment of High Court – Banking facility – Islamic financing – Bai' al-inah – Asset sale agreement and asset purchase agreement – Recovery of money due and payable – Failure to state asset used in transaction – Whether bai' al-inah contract in compliance with Syariah principle of financing*

Pursuant to a letter of offer dated 16 February 2009 ('first LO'), the respondent granted the first appellant a *bai' al-inah* financing facility with a ceiling limit of RM9,500,000 ('principal sum'). Following thereto, the respondent agreed to sell its asset to the first appellant for a payment of RM14,233,200 and the respondent shall repurchase the said asset for RM9,500,000. The said purchase was subject to the terms and conditions contained, amongst others, in the first LO, master facility agreement ('MFA'), asset sale agreement ('ASA') and asset purchase agreement ('APA') all dated 31 July 2009. Pursuant to the first LO, the first appellant agreed to pay the principal sum by way of instalments effective from the tenth month from the date of disbursement. The second appellant had guaranteed the due performance of the first appellant's obligations. When the first disbursement was made on 15 July 2009, the first appellant failed to make any payment of the principal sum by the prescribed time. Despite the event of default, the respondent allowed the financing to be rescheduled *vide* a supplemental letter of offer ('second LO') dated 18 April 2014. Notwithstanding that, the first appellant failed and neglected to pay the monthly instalments as agreed in the first and second LO. The respondent then instituted an action against the appellants. The appellants disputed the respondent's claim and counterclaimed against the respondent. The High Court Judge allowed the respondent's claim and dismissed the appellants' counterclaim. Hence the present appeal. The issue that arose for determination during appeal, *inter alia*, was whether the *bai' al-inah* transaction was Syariah non-compliant as the first LO, second LO, MFA, ASA, APA and other security documents did not state the asset involved in the transactions.

Held (allowing appeal with costs) A
Per Ahmadi Asnawi JCA delivering the judgment of the court:

(1) The essence of the *bai' al-inah* transaction entered into by the parties must be grounded upon the basic premise that it must involve the sale and buy back transactions of an asset of a seller. The existence of the asset in the transactions is imperative without which such contract is not B *bai' al-inah* contract, but something else outside the system. (para 25)

(2) At the time the security documents were executed on 31 July 2009, the underlying asset in the *bai' al-inah* contract did not appear to exist. In the MFA, ASA, and APA, the description of the asset merely referred C to 'as set out in letter(s) of offer (if any)'. There was no mention of any asset in the first and second LO. As such, there were uncertainties in the underlying feature of the said *bai' al-inah* contract *ie* the existence of the asset in the transactions. (para 33)

(3) The *Mudharabah* General Investment Certificate attached to the D inter-office memo could not have been the asset transacted as the same was not mentioned in the letters of offer, MFA, ASA and APA. Being an inter-office memo, it is doubtful whether the appellants had access to the same. Further, at the time of the first LO, this asset has yet to come into being. The said certificate was also endorsed with 'tidak boleh E dipindahmilik' which violated the condition of complete transferability of ownership of the said asset and valid possession (*qabd*) of the said asset. (para 34)

(4) What transpired in this case was not a *bai' al-inah* financing contract but something unknown in the Syariah financing system. Hence, the F respondent's remedy is also elsewhere and not under the *bai' al-inah* financing system. Since there was no specific appeal against the dismissal of the appellants' counterclaim, the trial judge's decision ought not to be interfered with. (para 35)

Bahasa Malaysia *Headnotes* G

Menerusi satu surat tawaran bertarikh 16 Februari 2009 ('LO pertama'), responden telah memberikan perayu pertama satu kemudahan pembiayaan *bai' al-inah* dengan had maksimum sebanyak RM9,500,000 ('jumlah pokok'). Berikutan itu, responden bersetuju menjual asetnya kepada perayu pertama dengan bayaran sebanyak RM14,233,200 dan responden akan membeli H semula aset tersebut dengan harga RM9,500,000. Pembelian tertakluk pada terma dan syarat, antara lain, dalam LO pertama, perjanjian kemudahan induk ('MFA'), perjanjian penjualan aset ('ASA') dan perjanjian pembelian aset ('APA') kesemuanya bertarikh 31 Julai 2009. Selaras dengan LO pertama, perayu pertama bersetuju membayar jumlah pokok secara ansuran I berkuat kuasa dari bulan kesepuluh dari tarikh pembayaran. Perayu kedua telah menjamin pelaksanaan kewajipan perayu pertama. Apabila pembayaran

pertama dibuat pada 15 Julai 2009, perayu pertama gagal melunaskan bayaran jumlah pokok dalam tempoh yang ditetapkan. Walaupun berlaku keingkaran, responden membenarkan pembiayaan semula dijadualkan semula melalui surat tawaran tambahan ('LO kedua') yang bertarikh 18 April 2014. Walau bagaimanapun, perayu pertama gagal dan cuai membayar ansuran bulanan seperti yang dipersetujui dalam LO pertama dan kedua. Responden seterusnya memulakan satu tindakan terhadap kedua-dua perayu. Perayu mempertikaikan tuntutan responden dan menuntut balas terhadap responden bagi kerugian yang dialami. Hakim Mahkamah Tinggi membenarkan tuntutan responden dan menolak tuntutan balas perayu. Oleh itu, rayuan ini. Isu yang dibangkitkan untuk pertimbangan semasa rayuan, antara lain, adalah sama ada transaksi *bai' al-inah* masih mematuhi prinsip Syariah walaupun LO pertama, LO kedua, MFA, ASA, APA dan dokumen sekuriti lain tidak menyatakan aset yang terlibat dalam transaksi tersebut.

Diputuskan (membenarkan rayuan dengan kos)
Oleh Ahmadi Asnawi HMR menyampaikan penghakiman mahkamah:

(1) Asas transaksi *bai' al-inah* yang ditandatangani pihak-pihak harus berdasarkan ciri asas bahawa ia mesti melibatkan transaksi jual dan beli balik aset penjual. Kewujudan aset dalam transaksi adalah penting kerana tanpanya kontrak tersebut bukanlah kontrak *bai' al-inah*, tetapi sesuatu yang lain daripada sistem.

(2) Semasa dokumen sekuriti dimeterai pada 31 Julai 2009, aset dalam kontrak *bai' al-inah* tidak wujud. Dalam MFA, ASA dan APA, perihal aset hanya dirujuk sebagai 'as set out in letter(s) of offer (if any)'. Tetapi tiada aset tidak dinyatakan dalam LO pertama dan kedua. Oleh itu, terdapat ketidaktentuan dalam ciri yang disandarkan dalam kontrak *bai' al-inah* tersebut iaitu kewujudan aset dalam transaksi.

(3) Sijil General Investment *Mudharabah* yang dikepilkan pada memo dalaman pejabat tidak boleh menjadi aset yang ditransaksikan kerana ia tidak dinyatakan dalam surat-surat tawaran, MFA, ASA dan APA. Sebagai memo dalaman pejabat, terdapat keraguan sama ada perayu mempunyai akses yang sama. Di samping itu, dalam LO pertama, aset ini masih belum wujud. Sijil tersebut juga diendorskan dengan 'tidak boleh dipindahmilik' yang melanggar syarat pindah milik lengkap aset dan milikan sah (*qabd*) aset tersebut.

(4) Apa yang dimeterai dalam kes ini bukan kontrak pembiayaan *bai' al-inah* tetapi sesuatu yang asing dalam sistem pembiayaan Syariah. Oleh itu, remedi responden juga adalah melalui cara lain dan bukan di bawah sistem pembiayaan *bai' al-inah*. Oleh kerana tiada rayuan spesifik terhadap penolakan tuntutan balas perayu, dapatan hakim bicara berkaitannya tidak wajar diganggu.

Other source(s) referred to:
Bank Negara Malaysia, *Syariah Resolutions in Islamic Finance,* 2nd edn, p 109

For the appellant - Zainal Azhar (Sukri & Melisa Sukri with him); M/s Zainal Azahar & Co
For the respondent - Wong Koh Hui (Renee Tiun with him); M/s Jeff Leong, Poon & Wong

[Editor's note: For the High Court judgment, please see Malaysian Debt Ventures Bhd v. FLH ICT Services Sdn Bhd & Anor [2014] 1 LNS 1349 (overruled)]

Reported by Sandra Gabriel

JUDGMENT

Ahmadi Asnawi JCA:

[1] In the court below, the respondent/plaintiff claimed against the first appellant/first defendant being the principal borrower and the second appellant/second defendant, the guarantor, for the recovery of monies due and payable under the Syariah financing facility known as *bai' al-inah* granted by the respondent to the first appellant.

[2] *Vide* its writ and statement of claim dated 2 August 2012, the respondent sought the following orders:

(a) Judgment for the sum of RM12,139,615.23;

(b) *Ta'widh* at 1% per annum or any rate as determined by the respondent on the sum of RM12,139,615.23 from 30 June 2011 till the date of full realisation;

(c) Cost on solicitor-client basis; and

(d) Any other relief deemed necessary by the court.

[3] The appellants hotly disputed the said claims upon various grounds and put forth their counterclaim against the respondent, amongst others, claiming for special damages in the sum of RM172 million as loss of profit suffered by the first appellant as a result of the termination of the *bai' al-inah* facility by the respondent, general, exemplary and punitive damages, interest at the rate of 4% per annum and costs.

[4] After a full hearing, on 21 March 2014 the learned judge allowed the respondent's claim as prayed as the respondent had succeeded to prove its claim against both the appellants on a balance of probabilities. The learned judge also dismissed both the appellants counterclaim and awarded RM50,000 costs to be paid by the appellants to the respondent. Hence this appeal before us.

A **The Background**

[5] Pursuant to the letter of offer dated 16 February 2009 ('first LO') the respondent had granted the first appellant *bai' al-inah* financing facility with a ceiling limit of RM9,500,000 (principal sum). Following thereto, the respondent agreed to sell its asset to the first appellant for a staggered payment of RM14,233,200 (sale price) and the respondent shall repurchase the said asset for RM9,500,000 (purchase price). The said purchase was subject to the terms and conditions contained in the first LO, the master facility agreement dated 31 July 2009 ("MFA"), deed of assignment dated 31 July 2009, ("DOA"), debenture dated 31 July 2009, asset sale agreement ("ASA") and asset purchase agreement ("APA") both also dated 31 July 2009 and the supplemental letter of offer dated 18 April 2014 ("second LO").

[6] The first appellant had agreed to accept the respondent's offer subject to the terms and conditions contained in the above said agreements.

[7] The *bai' al-inah* facility was for the purpose of constructing and developing a data centre facility for the Kelantan State Government as set out in Sch. 1 item 3 of the first LO dated 16 February 2009.

[8] It was also agreed that the first appellant was to pay profit rate for the said financing at 7% p.a calculated at daily rest to be calculated 12 months in advance for the first year. The profit for the following years shall be paid quarterly in advance.

[9] Pursuant to item 11 of Sch. 1 of the first LO, the first appellant had agreed to pay the principal sum by way of instalments effective from the tenth month from the date of disbursement.

[10] The second appellant had unconditionally and irrevocably guaranteed the due performance of the first appellant's obligations under the above said contracts/agreements pursuant to a personal/joint and several guarantee executed by the second appellant on 31 July 2009. The second appellant had also agreed to pay and settle all sums due and payable by the first appellant to the respondent, on demand subject to the terms and conditions stipulated in the said guarantee. The second appellant had also agreed upon demand to indemnify and keep indemnified the respondent all fees, costs, charges, damages and all liabilities incurred in the course of obtaining and seeking to obtain payments from the appellants.

[11] The first disbursement was made on 15 July 2009. Pursuant to item 11 Sch. 1 of the first LO, the tenth month would be the month of May 2010. The first appellant though did not make any payment of the principal sum on time as stated in the above Sch. 1.

[12] The first appellant only made the first payment in the sum of RM80,000 on 27 July 2010 and the second payment amounting to RM40,000 on 4 August 2010. Apparently an event of default had occurred and the respondent was entitled to stop further payments of the funds pursuant to the agreements.

[13] Despite the event of default and at the request of the appellants, the respondent had allowed the said financing to be rescheduled *vide* supplemental letter of offer dated 18 April 2014 (second LO) agreed and signed by both parties. The payment of the principal sum was rescheduled to commence on 31 August 2011. Following the second LO, a subsequent sum amounting to RM3,206,189 was disbursed to the appellants.

[14] The terms of the second LO also provided that the final sum of RM1,437,851 could only be disbursed once the data centre was completed upon receipt of the approval from the local authority on the conversion of land and upon acceptance of the certificate of fitness to occupy the premises.

[15] Despite having been allowed to reschedule its monthly repayment and despite further disbursements made pursuant to the second LO, the first appellant had failed and neglected to pay the monthly instalments as agreed in the first and second LO. The respondent then caused a notice to recall to be issued to both the appellants dated 18 July 2012.

[16] Despite a valid demand having been issued both the appellants had refused to comply with the said recall notice, thus prompting the respondent to institute this civil action against both the appellants.

The Appeal

[17] The appellants' appeal could broadly be grounded upon the following:

(a) the underlying asset in the *bai' al-inah* transaction does not exist;

(b) the respondent had no capacity and was not licensed to deal in this kind of transaction; and

(c) double profit was imposed which clearly contravened the most basic of the *bai' al-inah* principles.

[18] Only the first ground attracted our consideration.

[19] Learned counsel for the appellants submitted that the first LO, the second LO, the MFA, ASA, APA and other related security documents did not state the asset involved in the transactions therein and accordingly the parties are bound with what they had executed and cannot be rewritten for any omission. Hence the *bai' al-inah* transaction herein is Syariah non-compliant.

[20] Learned counsel further submitted that the introduction of an inter-office memo together with its Mudharabah General Investment Certificate No. 41098 issued on 26 May 2009 dated 13 July 2009 (see rekod rayuan - Jilid 3 Bahagian C(5) pp. 2720 - 2721) which in fact is a non-transferable fixed deposit in the sum of RM10 million as the asset used in the transactions was unrelated and an afterthought in contravention with the fifth condition on asset ownership and transferability (*qabd*).

[21] Additionally learned counsel submitted that the inter-office memo is only for the eyes of the respondent's staff internally and there was no way for the appellants to know that the same is the asset to be used in the transactions.

Our Decision

[22] The learned judge correctly alluded that in order to ascertain the validity of the agreements, one had to examine the features present in the *bai' al-inah* transaction as applied in this case. The resolutions by the Syariah Advisory Council (SAC) relating to the same are most pertinent. The *Syariah Resolutions in Islamic Finance* by Bank Negara Malaysia, 2nd edn (adverted to by the learned judge) states, at p. 109:

> Bai' 'Inah refers to a contract which involves sale and buy back transactions of an asset of a seller. In those transactions, the seller sells an asset to the buyer on cash basis and then buys back the asset at a deferred price, which is higher than the cash price. It may also be conducted where the seller sells the asset to the buyer at a deferred price and subsequently buys back the asset on cash basis at a lower price than the deferred sale price. Bai' 'Inah concept is used in Malaysian Islamic Banking and Islamic capital market system to fulfil the various needs of market players, mainly during the initial development state of Islamic financial system.

[23] The learned judge also alluded to the resolutions of the SAC's 16th meeting on 11 November 2000 and 82nd meeting on 17 February 2009 mandating the following conditions to validate a *bai' 'inah* contract (found at p. 113, *Shariah Resolutions in Islamic Finance* by Bank Negara Malaysia, 2nd edn):

(a) the contract must consist of two clear and separate contracts, namely a purchase and sale contract;

(b) no stipulated condition in the contract to re-purchase the asset;

(c) both contracts are concluded at different times;

(d) the sequence of each contract is correct, whereby, the first sale contract shall be completely executed before the conclusion of the second sale contract; and

(e) Transfer of ownership of the asset and a valid possession (*qabd*) of the asset in accordance with Syariah and current business practice ('*urf tijari*').

[24] The position was correctly summarised by the learned judge as follows: A

> ... the Bai Al-Inah contract shall consist of two clear and separate contracts termed as the Asset Sale Agreement ("ASA") and the Asset Purchase Agreement ("APA") respectively with no express provision or condition in the contract to repurchase the asset. The ASA and APA must stand B alone and not tied to one another. Both the ASA and APA must be concluded at different times, which meant that the ASA shall be completely executed before the conclusion of the APA. There must also be transfer of ownership of the asset and a valid possession of the asset in accordance with Shariah and current business practice.

C

[25] In our view the essence of *bai' al-inah* transaction or contract in the matter before us as entered into by the parties herein must necessarily be grounded upon the basic premise that it must involve the sale and buy back transactions of an asset of a seller. The existence of the asset in the transactions is an imperative without which such contract is not a *bai' al inah* D contract, but something else outside the Syariah system.

[26] We shall now investigate the relevant security documents.

[27] Item 4 of Appendix 1 of the APA (at pp. 405 to 409 of RR - Jilid 3 Bahagian BB) relating to the "description of the asset" states that the same is "as set out in letter(s) of offer (if any)". In the entire agreement this is the E only reference relating to the asset in issue. The APA is dated 31 July 2009.

[28] Item 4 of Appendix 1 of the ASA (at pp. 399 to 404 of the same jilid) speaks in similar terms in respect of the description of the asset. In the entire agreement this is the only reference relating to the asset in issue. The ASA is also dated 31 July 2009. F

[29] Section 1.02 of art. 1 of the MFA (found at pp. 303 to 398 of the same jilid) provides:

> In accordance with the financing procedure under the Shariah contract of Bai Al-Inah, MDV will sell the Asset (as defined herein) to the Customer G at the Asset Sale Price (as defined herein) on deferred payment basis and subsequently thereafter MDV will purchase back the asset from the customer at the Asset Purchase Price (as defined herein) upon the terms and conditions herein.

Meanwhile s. 2.01(a) of art. 2 provides the definition of asset: H

> "Asset" means the Shariah-compliant asset more particularly described in the Schedule 1A herein and "Asset" shall be construed accordingly.

Schedule 1A of the MFA provides the "description of asset" as "as set out in letter(s) of offer (if any)."

I

[30] We have tooth-combed the first LO, its schedules and appendixes (at pp. 197 to 216 of the same jilid). We could find no mention of any asset in the first LO to be transacted in the MFA, ASA and APA. We have similarly tooth-combed the second LO (at pp. 291 to 295 of the same jilid). There is equally no mention of any asset in the second LO to be transacted in the relevant MFA, ASA and APA.

[31] The issue of non-existence of the said asset was fiercely contested by the appellants in the court below. In respect of the same SP1, for the respondent who professed and appeared profoundly ignorant of the *bai al-inah* financing contract was evasive but finally said that the security documents does not state the asset in question.

[32] SP2 who also appeared immensely ignorant of *bai al-inah* contract finally agreed that the asset was not stated in the MFA, ASA and APA. The transactions were devoid of any asset. SP3 in his testimony did not at all mention any asset.

[33] On the factual matrix of the case enumerated above, it is apparent that at the time the security documents (MFA, ASA and APA) were executed on 31 July 2009, the underlying asset in the *bai' Al-Inah* contract does not appear to exist. At the risk of being repetitive, in the MFA and both the ASA and APA, the description of the asset were merely referred to "as set out in letter(s) of offer (if any)". As said earlier, the first and second LO did not mention any asset whatsoever. Hence it begs the question what actually was being transacted on 31 July 2009 between the seller and the purchaser in the MFA, ASA and APA. There are uncertainties in the underlying feature of the said *bai' al-inah* contract/financing ie, the existence of the asset in the transactions. Following through, hence the *akad* to sell and the *akad* to purchase the asset are not certain and distinct in the absence of the same, a fundamental requirement under the *bai' al-inah* contract.

[34] We are also of the view that the Mudharabah General Investment Certificate No. 41098 attached to the inter-office memo (at pp. 2720 to 2721 RR - Jilid 3 Bahagian C5) could not have been the asset transacted on account that, firstly, the same was not mentioned in the LOs, the MFA, the ASA and APA. Neither was there any indication that the said certificate is intended to be the asset in the said transactions. Secondly, it was attached to an inter-office memo which is obviously for internal circulation only. Being an inter-office memo, it is doubtful whether the appellants had access to the same. It was the appellants' case that they knew nothing about the existence of the said certificate. Thirdly, the certificate was issued on 26 May 2009 and dated 13 July 2009. Obviously it predated the execution of the MFA, ASA and APA. As such if the certificate was intended to be the asset in the said transactions, then the parties should encounter no difficulty in naming the same as the asset in the MFA, ASA and APA. Obviously this was not done. It is also obvious that at the time of the first LO (dated 16 February 2009), this asset has yet to come into being. Otherwise it would have been stated

in the first LO. Finally, the said certificate was endorsed with the endorsement "Tidak Boleh Dipindahmilik (Not Transferable)". In such event, the ownership of the asset cannot be transferred to the purchaser. The said endorsement plainly violated the condition of complete transferability of ownership of the said asset and valid possession (*qabd*) of the said asset in accordance with Syariah and current business practice ('*urf tijari*') as resolved by the resolution of the SAC adverted to in para. 22 above.

[35] In our view what had transpired obviously had violated the entrenched principles of *bai' al-inah* contract as stated in paras. 21 and 22 enumerated earlier which the learned judge herself had alluded to. It is neither Syariah compliant. As such it is not a *bai' al-inah* financing contract but something else unknown in the Syariah financing system. Hence the respondent's remedy is also elsewhere and not under the *bai' al-inah* financing system. The respondent cannot take advantage of the system when the contract they entered into is unknown in the system.

Counterclaim Of The Appellant At The High Court

[36] The appellant had brought a counterclaim against the respondent (paras. 28 to 53 pernyataan pembelaan terpinda dan tuntutan balas terpinda) for "ganti rugi khas berjumlah RM172 juta sebagai kerugian/keuntungan (loss of profit) yang ditanggung oleh defendan pertama, ganti rugi am, ganti rugi teladan, ganti rugi punitative" interest and costs. The learned judge had dismissed the counterclaim on the grounds that the appellants had failed to prove their counterclaim on the standards required by law (para. 86 of the grounds of judgment).

[37] We note that the notis rayuan filed by the appellants was only against the whole of the decision that allowed the respondent's claim in the sum of RM12,139,815.23 until 30 August 2012 with cost. There was as such no appeal brought against the dismissal of the appellants' counterclaim. Notwithstanding that, the appellants in their written submissions filed in this appeal included submissions on why their counterclaim should be allowed. This however was not pursued in the oral submissions before us.

[38] From the pleadings of the appellants the counterclaim was allegedly for projected loss of profit over a 30 year period arising from "breach of contract" by the respondent. The evidence on this before the trial court was merely "calculations" and estimates (reduced to RM46 million in their written submissions).

[39] In our view since there was no specific appeal against the dismissal of the appellants' counterclaim, the learned judge's decision thereto ought not to be interfered with. In any event it was also our view that the learned judge did not err in disallowing the counterclaim as it was not supported by any concrete evidence of loss suffered or likely to be suffered by the appellants apart from being purely based on remote possibilities and conjectures only.

A

Conclusion

Accordingly

[40] The appeal of both the appellants against the decision of the High Court of 21 March 2014 ordering judgment in favour of the respondent is
B allowed with costs.

[41] Orders of the High Court that the appellants pay the respondent:

(a) Jumlah wang sebanyak RM12,139,615.23 setakat 30 June 2012;

(b) Kos pampasan pada kadar 1% setahun atau pada kadar lain yang
C ditetapkan oleh plaintif ke atas RM12,139,615.23 mulai 30 June 2012 sehingga tarikh penyelesaian penuh; dan

(c) Kos sebanyak RM50,000.

are hereby set aside.

D **[42]** The order of the High Court dismissing the counterclaim of the appellants is affirmed.

[43] Having heard parties further on costs and taking into particular consideration that the appellants' counterclaim had been dismissed by the High Court and such dismissal had been affirmed by us, we award the
E appellants costs here and below in the overall sum of RM30,000.

[44] Deposit to be refunded.

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